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Supreme Court, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1971

No. 71-703

UNITED STATES OF AMERICA,

Appellant,

v.

FIRST NATIONAL BANCORPORATION, INC. and THE FIRST NATIONAL BANK OF GREELEY,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLORADO

ANSWER OF APPELLEES TO BRIEF FOR THE FEDERAL DEPOSIT INSURANCE CORPORATION AS *AMICUS CURIAE*

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Washington, D. C. THIEL PRESS 202 393-0625

TABLE OF CITATIONS

Page

Cases:

Duran v. United States, 413 F.2d 596 (9th Cir. 1969), cert. denied, 396 U.S. 917 4

Heath v. Helmick, 173 F.2d 156 (9th Cir. 1949) 4

Lawn v. United States, 355 U.S. 339 (1958), reh. denied, 355 U.S. 967 5

McClellan v. Carland, 217 U.S. 268 (1910) 4

Panaview Door and Window Co. v. Reynolds, 255 F.2d 920 (9th Cir. 1958) 4

Sterns v. Hertz Corp., 326 F.2d 405 (8th Cir. 1964), cert. denied, 377 U.S. 934 4

United States v. Addonizio, 449 F.2d 100 (3rd Cir. 1971) 4

United States ex rel. Collins v. Ashe, 176 F.2d 606 (3rd Cir. 1949) 4

Watson v. Rhode Island Ins. Co., 196 F.2d 254 (5th Cir. 1952) 4

Administrative Decision:

First United Bancorporation, Inc. (Fort Worth, Texas), Order Approving Acquisition of Bank, 6/26/72, 1972 Fed. Res. Bull.___ 6

Statutes:

Clayton Act, Section 7, 15 U.S.C. §18, 38 Stat. 731 . . . . . 1, 2

12 U.S.C. §2, 49 Stat. 707 2

Miscellaneous:

Assets and Liabilities–Commercial and Mutual Savings Banks, Federal Deposit Insurance Corporation, June 30, 1971 7

Bank Operating Statistics, 1970, Federal Deposit Insurance Corporation 7

Bell and Murphy, Economies of Scale in Commercial Banking, *Administrative Decision*: Federal Reserve Bank of Boston, 1967 8

Defendant's Opening Memorandum in Support of Motion for Judgment on the Record, Washington Mutual Savings Bank, et al. v. Federal Deposit Insurance Corp., No. 45 - 71 C 3, W.D. Wash. 2

Llewellyn, The Common Law Tradition–Deciding Appeals (1960) 4

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The Federal Deposit Insurance Corporation (the "FDIC") has filed an *amicus curiae* brief in support of the position of the Department of Justice (Appellant), arguing that the Clayton Act ought to be interpreted to reach a very broad class of cases where the probable competitive effects are conjectural and prospective rather than direct and immediate. Since the FDIC has taken the unequivocal position that it can reject merger proposals on competitive grounds even when they do not violate

the standards of the Sherman or Clayton Act,[1] it seems clear that its brief is designed to impose those interpretations, not on itself, but rather on the other bank regulatory agencies.

The brief *amicus* for the FDIC in this case states broadly that in Section 7 cases alleged to involve the elimination of a prospect of substantial future competition between affiliating banking organizations, this Court should: (1) ignore "subjective" evidence, (2) use only "objective" evidence, (3) ignore the expressed policy of the responsible regulatory agency (if that agency would *not* charter new banks) because of the transitory status of policy makers,[2] (4) look to state markets and (5) finally, contends that there are no relevant economies of scale in holding company acquisitions.

The first four briefing points are arguments; they do not differ materially from the same arguments as articulated by the Appellant herein and the Court is respectfully referred to the principal briefs for a consideration of the merits of these contentions.

The fifth point, and the purpose for which we assume the brief was filed, makes representations of fact. It is

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[1] Defendant's Opening Memorandum in Support of Motion for Judgment on the Record at 2, *Washington Mutual Savings Bank, et al. v. Federal Deposit Insurance Corporation* (No. 45-71C3, W.D. Wash.).

[2] This curious claim relates, in context, to a Comptroller of the Currency who is in the first year of a second five year term (12 U.S.C. §2, 49 Stat. 707) and a State Bank Commissioner with statutory life tenure (App. 493).

contended that this acquisition would not occasion any appreciable economies of scale.[3]

There was testimony in this case by experts for *both* sides as well as industry members that there are significant economies of scale associated with holding company growth.[4]

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[3] "However, as the size of a banking *organization* expands through the acquisition of additional offices, no appreciable economies of scale occur." (emphasis in original) (at 17).

[4] *Baxter*, App. 430: "Q. Are there economies of scale which these banking organizations could obtain in operating these—operating in these communities? A. Yes, I think there are. Q. Could you support that conclusion? A. Well, larger banking organizations—it can be demonstrated from various studies that have been done—do enjoy lower unit costs of operation. If one looks at economy of scale as being the unit cost of producing a given output, the larger banking organizations with branch banking facilities or holding companies could take advantage of these lower unit operating costs and would pass on these advantages—competition would induce them, indeed, force them to pass on these advantages and these cost savings that they achieve . . . .

App. 432: "Now most economists I would say, including one of plaintiff's experts, Dr. Hall, have stated that there are competitive advantages to more liberal branching and holding company movements. These competitive advantages incorporating the economies of scale [then discussing several studies]."

Hall, App. 239: "Q. Now, Dr. Hall does correspondent banking have an important economic function? A. Yes, it's in a country which has a lot of banks—small banks which are either unit banks or small holding companies or small branch bank systems. The fact that these banks *can obtain access to the facilities of large banks, facilities where there are economies of scale* are important for making the system work." (emphasis supplied).

Moon, App. 162-163: Q. Mr. Moon, was your principal and primary reason for starting the Affiliated Bankshares the desire of the members of your organization to take advantage of the economies of scale attendant upon a holding company structure? . . . A. I find it difficult to answer yes. This was certainly a major consideration."

The FDIC takes issue with this testimony and offers its own arguments. However, an appeal should not be the occasion for injection of new and untested factual data into the record. One of the "steadying factors in appellate courts" is "a frozen record from below."[5] A long line of federal cases clearly establishes the principal that an appellate court may only consider facts of record. *United States v. Addonizio*, 449 F.2d 100, 103 (3rd Cir. 1971); *Duran v. United States*, 413 F.2d 596, 605 (9th Cir. 1969), cert. denied, 396 U.S. 917; *United States ex. rel. Collins v. Ashe*, 176 F.2d 606 (3rd Cir. 1949); *Stearns v. Hertz Corp.*, 326 F.2d 405, 408 (8th Cir. 1964, cert. denied, 377 U.S. 934; *Watson v. Rhode Island Ins. Co.*, 196 F.2d 254, 256 (5th Cir. 1952). This is so even if matters not before the trial court have been included in the record by stipulation. *Panaview Door and Window Co. v. Reynolds*, 255 F.2d 920 (9th Cir. 1958); *Heath v. Helmick*, 173 F.2d 156 (9th Cir. 1949). Even in the case of an affidavit and papers filed with this Court by a trial judge containing matters which were not in the record before him, this Court has stated (*McClellan v. Carland*, 217 U.S. 268, 283 (1910)):

> "We shall not enter upon a consideration of these papers because they are not in the record, as the same has been certified to us from the circuit court of appeals as the one upon which it acted . . . .
>
> . . . We must take the case as it is presented here upon the stipulated return to the writ of certiorari on the record as presented to the circuit court of appeals."

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[5] Llewellyn, *The Common Law Tradition–Deciding Appeals*, 28 (1960).

More recently in *Lawn v. United States*, 355 U.S. 339, 354 (1958), reh. denied, 355 U.S. 967, the Court granted a motion to strike a grand jury transcript proffered by the government and portions of the government's brief relating thereto, stating, "we must look only to the certified record in deciding questions presented." We think it is likewise clear that Appellant may not indirectly, through the offices of an "amicus curiae," bring before the Court assertions of fact of any kind, much less assertions which directly take issue with the record in the case.

Moreover, the FDIC's arguments are internally inconsistent. An economy of scale is an advantage inhering in larger size which permits the beneficiary to offer a better product at the same price or the same product at a better price or both. The FDIC argues that no such advantages may be found in accretions of banking offices to a holding company (at 20) yet on the very same page complains of the unfair advantages accruing to a new holding company affiliate by reason of its ability to offer more sophisticated services at comparable prices:

> Large banks have several advantages, since the same operating expense ratios as a smaller bank would permit the larger bank to spend more dollars for particular functions and yet show the same degree of profitability.[6]

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[6] The FDIC also contends that advertising advantages of size would permit a larger bank to garner more of the area business. Once again, the FDIC is attempting to rewrite the record. There was uncontested evidence below that there were no economies of scale in market diffusion advertising in banking and that, in any event, advertising was a very modest portion of bank budgets (as distinct from many industries), so that holding company acquisitions in new geographic areas would not ride the advertising

On its own claim then, the FDIC not only concedes but complains of the major economies of scale associated with large banking systems.[7] The Federal Reserve Board has also publicly acknowledged "the service advantages growing out of the greater efficiencies that are characteristic of a holding company affiliation." (*First United Bancorporation, Inc.* (Fort Worth, Texas), Order Approving Acquisition of Bank, 6/26/72, at 4 (1972 Fed. Res. Bull.___)). And since the Comptroller of the Currency has filed an amicus brief in this case specifically taking issue with the claim of "no appreciable economies," there appears to be unanimity among the bank regulatory agencies that holding company affiliations *do* yield significant economies of scale.

It is apparent that the FDIC means something else when it speaks of "economies of scale" than did the experts who testified in this case and something different from the general understanding of the term as set out above. The FDIC is limiting its inquiry on available economies to mechanical functions performed within a bank, and only to certain mechanical functions at that.[8] Larger organizations hire specialized personnel and invest

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coattails of the parent. There was some indication that such an attempt might even be counterproductive (App. 397, 1382-1384). We assume that an *ipse dixit* of an appeal level amicus will not be permitted to supplant the trial record herein.

[7] Implicit in this complaint is a recognition that such economies are not resolvable through the correspondent system.

[8] Appendix B of the FDIC brief makes it clear that no analysis was made of computer service costs, capital funds and "all other" expenses. They were assumed to be the same as the average of calculated factors. No basis for the assumption is offered.

in equipment providing higher quality service (*e.g.*, sophisticated data processing) all to the benefit of the consumer. Such efficiencies are masked by the sort of analysis advanced here.

We do not believe that any more need be said regarding the FDIC brief. In the main, it is a redundancy. Where it does serve Appellant's purpose it does so by asserting a conclusion of fact (no scale economies) totally at odds with the record made below. For that reason alone, it merits no consideration on these deliberations. Even on its own terms, however, the claim deteriorates to a semantic quibble.

Passing this second hurdle, *arguendo*, the presentation is technically flawed since even within its own limited frames of references, the contention does not sustain Appellant's root conclusions regarding the utility of more banking offices in Greeley nor the concept that Bancorporation ought find *de novo* entry attractive. We have not the materials upon which the FDIC's three to fifteen bank, $150 million asset market model was constructed so that we cannot now test its accuracy. Assuming its validity, the model yields economies of scale of $495,000 between a market occupancy of 3 and 15 banks. But banks with $150 million in assets would have a deposit base of about $125 million[9] and would be expected to earn up to $1,250,000 between them.[10] Thus, in the

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[9] All commercial banks in the United States as of June 30, 1971, had assets of $600 billion and deposits of $504 billion. (*Assets and Liabilities–Commercial and Mutual Savings Banks*, Federal Deposit Insurance Corporation, June 30, 1971).

[10] All commercial banks in the United States held year end deposits in 1970 of $435 billion and net pre-tax earnings for the year of $4.33 billion (*Bank Operating Statistics, 1970*, Federal Deposit Insurance Corporation).

FDIC's mechanical economies model, there are scale economies of up to 40% of net earnings.[11]

To place the impact of these kinds of funds in a meaningful context, $495,000 would support two new computer programmers, two additional trust officers, two new real estate specialists and four additional drive-in tellers at each of the three banks in addition to a 10% rise in dividends to all shareholders.

Standing alone, these mechanical scale efficiencies are not insignificant. Together with the efficiencies inhering in staff and service upgrading–also conceded by the FDIC–they offer a strong factual basis for the contention they purport to refute. Appellant has argued–fundamentally–that, however many banks there may be in a given market, the interests of the public are better served if we enhance the prospect that, someday, there can be "one more."

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[11] Bell and Murphy, on whose work the FDIC brief draws heavily (at 18-19) state:

> "Economies of scale are evident in commercial banking and arise through specialization of labor or machines or both. Of all commercial banking functions, demand deposits make the greatest use of machines. The kind used for this function changes with the level of output. Productivity differences among the machines contribute to the economies of scale. Except for demand deposits, banking functions are relatively labor intensive, with scale economies resulting predominantly from labor specialization. As more operations become computerized, these functions may grow more capital intensive . . . " (*Economies of Scale in Commercial Banking*, Federal Reserve Bank of Boston, 1967, p. 19).

The mechanical scale efficiencies seriously compromise Appellant's "one more is better" argument, while the staff and service improvements refute the FDIC thesis.

Respectfully submitted,

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July, 1972